

STATE OF TENNESSEE

Office of the Attorney General **RECEIVED**



2003 JUN 27 PM 2:36

T.R.A. DOCKET ROOM

ANDY D. BENNETT
CHIEF DEPUTY ATTORNEY GENERAL

LUCY HONEY HAYNES
ASSOCIATE CHIEF DEPUTY
ATTORNEY GENERAL

PAUL G. SUMMERS
ATTORNEY GENERAL AND REPORTER

MAILING ADDRESS

P.O. BOX 20207
NASHVILLE, TN 37202

MICHAEL E. MOORE
SOLICITOR GENERAL

CORDELL HULL AND JOHN SEVIER
STATE OFFICE BUILDINGS

TELEPHONE 615-741-3491
FACSIMILE 615-741-2009

Reply to:
Consumer Advocate and Protection Division
Post Office Box 20207
Nashville, TN 37202

June 27, 2003

Honorable Sara Kyle
Chairman
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243

RE: In Re: Petition of Tennessee American Water Company to Change and Increase Certain Rates and Charges So As to Permit it to Earn a Fair and Adequate Rate of Return on Its Property Used and Useful in Furnishing Water Service to Its Customers
Docket No. 03-00118

Dear Chairman Kyle:

Enclosed is an original and thirteen copies of a Proposed Settlement Agreement between the Attorney General and Tennessee American Water Company. Copies are being sent to all parties of record. If you have any questions, kindly contact me at (615) 532-3382. Thank you.

Sincerely,

Vance Broemel
Assistant Attorney General

Enclosures
cc: All Parties

64720

**IN THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

IN RE:

**PETITION OF TENNESSEE-AMERICAN
WATER COMPANY TO CHANGE AND
INCREASE CERTAIN RATES AND
CHARGES SO AS TO PERMIT IT TO EARN A
FAIR AND ADEQUATE RATE OF RETURN
ON ITS PROPERTY USED AND USEFUL IN
FURNISHING WATER SERVICE TO ITS
CUSTOMERS**

)
)
) **DOCKET NO. 03-00118**
)
)
)
)
)
)
)
)
)

PROPOSED SETTLEMENT AGREEMENT

For the sole purpose of settling the case of Petition of Tennessee-American Water Company to Change and Increase Certain Rates and Charges So as to Permit It to Earn a Fair and Adequate Rate of Return on its Property Used and Useful in Furnishing Water Service to its Customers, TRA Docket No. 03-00118, the Office of Attorney General through the Consumer Advocate and Protection Division (hereinafter "Attorney General") and Tennessee-American Water Company ("Tennessee-American") hereby agree and stipulate as follows in the above-styled case set for hearing on June 30, 2003:

1. The Attorney General and Tennessee-American stipulate and agree that Tennessee-American is entitled to earn a 7.73% return on investments with a 9.9% return on equity, as shown in attached Schedule 1.
2. The Attorney General and Tennessee-American further stipulate and agree that a 7.73% return on investment generates a revenue deficiency of either: (1) \$1,617,447 in the event the Tennessee Regulatory Authority continues to impute the reduction of the fire hydrant annual

charges as ordered by the TRA in its response to the Company's petition to voluntarily reduce its annual price for public fire service from \$301.20 to \$50 per public fire hydrant, in TRA Docket No. 99-00891; or (2) \$2,745,411 in the event the TRA decides to reverse the imputation of the fire hydrant annual cost or otherwise approve an overall settlement with an adjustment that would offset the loss in public fire service revenues. The revenue deficiency with and without the imputation of the fire hydrant annual cost is shown in Schedule 2.

3. The Attorney General and Tennessee-American further stipulate and agree that Tennessee-American shall withdraw its request for the "Distribution System Renewal Surcharge" as set forth in its proposed tariff.

4. In the event that the TRA does not accept the Proposed Settlement in whole or in part, the Attorney General and Tennessee-American are not bound by any position set forth herein.

TENNESSEE-AMERICAN WATER
COMPANY

BY: *R. Dale Grimes*

R. Dale Grimes (BPR# 6223)
BASS, BERRY & SIMS PLC
(615) 742-6200

BY: *T.G. Pappas*

T.G. Pappas (BPR #2703)
BASS, BERRY & SIMS PLC
(615) 742-6200

CONSUMER ADVOCATE AND
PROTECTION DIVISION OF THE
OFFICE OF THE TENNESSEE

ATTORNEY GENERAL

BY: *Vance L. Broemel*
Vance L. Broemel (BPR#11421)

Assistant Attorney General

(615) 741-8733

BY: *Shilina B. Chatterjee*

Shilina B. Chatterjee (BPR#20689)

Assistant Attorney General

(615) 741-3382

Dated: June 27, 2003

CERTIFICATE OF SERVICE

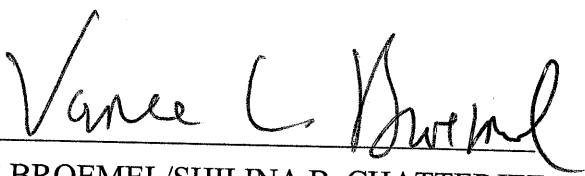
I hereby certify that a true and exact copy of the foregoing has been forwarded by facsimile and/or first-class mail, postage prepaid on June 26, 2003, to the following:

T.G. Pappas, Esq./Dale Grimes, Esq.
Bass, Berry & Sims, PLC
AmSouth Center
315 Deaderick Street, Suite 2700
Nashville, TN 37238-3001

Michael A. McMahan, Esq.
Phillip A. Noblett, Esq.
Lawrence W. Kelly, Esq.
Nelson, McMahan & Noblett
801 Broad Street, Suite 400
Chattanooga, TN 37402

Henry M. Walker, Esq.
Boult, Cummings, Conners & Berry, PLC
414 Union Street, Suite 1600
Nashville, TN 37219

David C. Higney, Esq.
Grant, Konvalinka & Harrison, P.C.
633 Chestnut Street, 9th Floor
Chattanooga, TN 37450


VANCE BROEMEL/SHILINA B. CHATTERJEE

Assistant Attorney General

June 27, 2003

Tennessee-American Water
Cost of Capital
For the 12 Months Ending March 31, 2004

Line No.	Parent:	Ratio	Cost	Weighted Cost
1	Common Equity	56.00%	9.90%	5.54%
2	Debt	44.00%	6.00%	2.64%
3	Total	<u>100.00%</u>		<u>8.18%</u>
	<u>Tennessee American:</u>	<u>Ratio</u>	<u>Cost</u>	<u>Weighted Cost</u>
4	Short Term Debt	6.2%	3.50%	0.22%
5	Long Term Debt	20.8%	7.62%	1.59%
6	Preferred Equity	1.6%	5.01%	0.08%
7	Common Equity	71.4%	8.18%	5.84%
8	Total	<u>100.00%</u>		<u>7.73%</u>

Source: Dr. Brown Workpapers and Co. Exhibit PRM-2, Schedule 1

Tennessee-American Water
Results of Operations
For the 12 Months Ending March 31, 2004

Line No.		CAPD		Company	F/	Difference
1	Rate Base	87,062,756	A/	87,270,579		(207,823)
2	Operating Income at Present Rates	5,098,465	B/	5,193,431		(94,966)
3	Earned Rate of Return (Line 2/Line 1)	5.86%		5.95%		-0.09%
4	Cost of Capital	7.73%	C/	8.559%		-0.83%
5	Required Operating Income (Line 1*Line 4)	6,729,951		7,469,489		(739,538)
6	Operating Income Deficiency (Line 5-Line 2)	1,631,486		2,276,058		(644,572)
7	Gross Revenue Conversion Factor	1.682767	D/	1.698908		(0.016141)
8	Normal Revenue Deficiency (Line 6*Line 7)	2,745,411		3,866,812		(1,121,401)
9	Fire Protection Rate Discount	(1,127,964)	E/	-		(1,127,964)
10	Rate Increase Needed if fire protection revenues continue to be imputed (Line 8-Line 9)	1,617,447		3,866,812		(2,249,365)
11	Current Rates	28,952,397				
12	% increase (Line 11 / Line 10)	5.5866%				
13	Rate increase if fire protection discount charged to all customers (Line 8)	2,745,411				
14	% increase (Line 13 / Line 11)	9.4825%				

A/ CAPD Exhibit, Schedule 2
B/ CAPD Exhibit, Schedule 3
C/ CAPD Exhibit SB__, Schedule 16
D/ CAPD Exhibit, Schedule 8
E/ TRA Order on 9/26/00 in Docket 99 - 00891
F/ Company SAV Exhibit 1, Schedule 1